

# TREASURY NEWS

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TREASURY DEPUTY ASSISTANT SECRETARY FOR  
FEDERAL FINANCE ROGER L. ANDERSON  
HOUSE BANKING AND FINANCIAL SERVICES SUBCOMMITTEE  
ON GENERAL OVERSIGHT AND INVESTIGATIONS

I appreciate the opportunity to discuss the Treasury's audit plan for studying the uses and counterfeiting of U.S. currency overseas. I have worked closely with the other members of the ACD Steering Committee to produce this plan, and we have already started to implement it.

As Under Secretary Hawke mentioned, two of the primary reasons for the successful introduction of the Series 1996 \$100 note were our comprehensive worldwide public education campaign and the coordination with our counterparts overseas. An especially important element in each of these areas was our International Currency Awareness Program or "ICAP." This program organized joint Treasury, Secret Service, and Federal Reserve teams to visit selected regions throughout the world to meet with U.S. embassy, foreign government, financial institution, and law enforcement officials to discuss the uses, flows, and counterfeiting of U.S. currency. Our teams made six trips over a two-year period to South America, Russia and the NIS, Southeast Asia, Western Europe, and the Middle East.

These trips enabled us to gain valuable information about the nature of U.S. currency usage and counterfeiting overseas. In addition, we were able to introduce the currency redesign program, assess the needs for our education campaign, and insure that there exists an adequate distribution network for the issuance of the new notes. Along the way, we established or augmented our working relationships with various entities involved in the overseas U.S. currency market.

The Antiterrorism and Effective Death Penalty Act requires us to audit the international

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use and counterfeiting of U.S. currency every three years. We have used our experience from ICAP as well as the past work of the ACD Steering Committee as a foundation for our Audit Plan. This experience is particularly relevant because the questions that the Act requires the audit to answer are some of the same questions that the ACD Steering Committee has examined and continues to examine on a regular basis. These are:

- o What are the uses and holdings of U.S. currency overseas?
- and
- o What is the Treasury's estimate of the amount of counterfeit U.S. currency that circulates outside of the United States each year?

We began to formulate our plan early on. In fact, as we worked with your staff, Mr. Chairman, to help draft the Act, we determined that our ICAP experience would provide a good starting point. The objectives of the audit plan, however, are decidedly different. Rather than introducing the new currency and insuring adequate distribution channels, we are now focusing more on the uses of U.S. currency and the quantities of genuine and counterfeit U.S. currency that are in circulation around the world.

Before finalizing our plan, we sought comment from GAO to insure that our plan provided all necessary information and detail. Unfortunately, after providing a draft of the plan to GAO, we were informed that they would be unable to give us comments because of a potential conflict of interest.

At your request, Mr. Chairman, GAO then commented formally on our plan, and we responded to their comments in an addendum to the plan. I have attached as an exhibit to my testimony a chronology of the development of our audit plan.

As we discussed in our plan and in the addendum, the Steering Committee is using a variety of information to try to answer the Act's questions.

The best sources of information to answer the first question are our surveys. Since last September, we have conducted two surveys in Southeast Asia and one in South America. Furthermore, we have scheduled four subsequent surveys on an approximately quarterly basis to include Turkey and Central Asia, Eastern and Central Europe, the Caribbean and Latin America, and India and Pakistan before we submit our first audit report in the fall of 1999. These trips greatly augment our understanding of currency movements outside of the wholesale banking sector.

The most important and comprehensive information to answer the second question comes from the Federal Reserve's currency shipment and receipt data. From these data, the Fed is able

to trace flows of U.S. currency throughout the world and identify the country of origin for deposits of both genuine and counterfeit U.S. currency.

In a statement to this Subcommittee last year, Theodore Allison, Assistant to the Board of Governors of the Federal Reserve System, described the Federal Reserve's currency processing operations.<sup>1</sup> I wish to highlight today three points from that statement:

- o First, the Federal Reserve receives a sufficient quantity of currency to have an up-to-date and reasonably accurate view of the notes in circulation. For example, during 1995 the Federal Reserve received from circulation, and therefore performed a note-by-note inspection of, a quantity of \$100 notes equal to 116 percent of all of the \$100s estimated to have been held within the United States and 13 percent of the \$100s held outside the country.
- o Second, the levels of counterfeit \$100 notes detected during 1995 were very low - less than one one-hundredth of one percent (.0075%) or 75 counterfeits in every one million \$100 notes inspected. Deposits of \$100s at the Federal Reserve that originated outside the United States had a lower proportion, about 55 counterfeits in every million notes processed.
- o Third, the successful passing of counterfeits, within the United States and abroad, is so small as to be insignificant from a macroeconomic perspective, and has no discernable effect on public confidence in U.S. currency.

I can now update Mr. Allison's numbers. In 1996, the percentages of domestically and internationally circulating \$100 notes that the Fed inspected increased to about 117 percent and 17 percent, respectively. Our window on counterfeiting therefore became even better last year, particularly in regard to counterfeits circulating outside the United States. That window showed, during 1996, a slight decline in counterfeit \$100s in circulation, as the detection rate fell from about 75 counterfeits per million notes processed (.0075%) to about 62 counterfeits per million (.0062%).

We consider the data from Federal Reserve currency processing operations to be reliable indicators of counterfeiting activity for several reasons:

- o The data are broadly based. The Reserve Banks made cash payments during 1996 that were destined for, and received deposits originating from, more than 80 countries.

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<sup>1</sup> Statement of Theodore E. Allison before the Subcommittee on General Oversight and Investigations of the Committee on Banking and Financial Services, U.S. House of Representatives, February 27, 1996, reprinted in Federal Reserve Bulletin, vol. 82 (April 1996), pp. 320-322.

- o The sample is very large. The Reserve Banks received and were thus able to inspect 17 percent (or one of every six) of all \$100 notes in circulation outside the United States during 1996.
- o Federal Reserve figures are similar to other available data. The incidence of counterfeits in notes received by Federal Reserve currency operations is very similar to that found by major wholesale commercial banks.

During 1996, the Federal Reserve improved its method of collecting data on banknote shipments to and from locations outside the United States. For cash payments by the Reserve Banks to depository institutions that intend to forward the banknotes to branches or customers abroad, participating institutions are now asked to identify each ultimate country of destination. Likewise, for cash deposits at Reserve Banks, participating institutions are asked to identify, for each 100-note strap of banknotes, the country from which the deposit originated. As a consequence, the usefulness of the Federal Reserve's operating data in making judgments about the geographic distribution of U.S. currency outside the United States has been enhanced. Similarly, the Fed's ability to provide to the Secret Service information on the country of origin of any counterfeits detected in deposits originating abroad improves the Service's understanding of the nature and extent of counterfeit U.S. currency that has been passed in various parts of the world.

As a result, we believe the Fed's data allow us to derive reasonable estimates of the amount of genuine and counterfeit U.S. currency that circulates outside of the country at any one time.

Of course, these estimates assume that the sample of currency the Fed receives each year is representative of the entire stock of U.S. currency in circulation. We have used the ICAP and subsequent overseas audit surveys to assess the validity of that assumption. We have focused particularly on this issue since our audit surveys began last fall. To date, without exception, the evidence has indicated that the sample is representative. We have seen nothing to suggest nor have we been given any plausible explanation for a process by which a significant amount of U.S. currency, counterfeit or otherwise, can circulate for an extended period of time without entering the banking system and eventually the Federal Reserve.

While it is impossible to know at any one time the precise amount of counterfeit currency in circulation, we are confident that the information we review on a continuous basis allows us to ascertain the magnitude of the counterfeiting problem. This information clearly shows that the counterfeiting of U.S. currency remains a de minimis economic problem, with the odds being minuscule of any particular individual actually incurring a loss due to counterfeiting. Nevertheless, we take counterfeiting seriously, as evidenced by the Secret Service's zero-tolerance approach to this crime.

Before concluding, I would like to mention some additional things we have learned from ICAP and the overseas audit surveys.

First, what we have found consistently, in addition to a wide variety of reasons for why people use U.S. currency, is that those individuals serve as an effective front line against counterfeiting. Foreign users of our currency are keenly aware of its features, and cash handling professionals are quite adept at detecting counterfeits. As the figures presented above illustrate, the counterfeit detection rates in foreign-origin currency deposits at the Fed have consistently been below the detection rates in domestic Fed deposits.

Second, one of the most important benefits of these programs is the opportunity to build and strengthen our relationships with our counterparts overseas. This has proven to be especially important for our introduction of newly designed currency and in countries where official government relations are still developing. In that regard, I can report that the Secret Service continues to work with the State Department to meet its overseas staffing needs. Over the past four months, the Service has received approval for five additional overseas positions.

Third, even though most of the people with whom we meet are anxious to provide any information they can, the vast majority do not track closely or focus upon U.S. currency usage in their own countries. Furthermore, most are under no obligation to provide us with information. Nevertheless, we believe that the vast majority give us the best information available.

In summary, the news that we have to report is good. The introduction of the \$100 has gone well; we are making preparations for the issuance of the newly designed \$50 this fall and the \$20 next year; we are well into the overseas currency audit process; we continue to build productive relationships with our counterparts overseas; and the information we have gathered thus far has held up in support of our estimates of worldwide counterfeiting levels. Nevertheless, we will continue to look critically at all of the available information.

We will also continue to look forward and take steps that will allow us to remain ahead of the counterfeiting threat -- a threat that will no doubt be with us for as long as our currency serves as the standard for stability and acceptability throughout the world.